

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

IN THE MATTER OF the Joint Application of	)	UTILITY DIVISION
NorthWestern Corporation and Babcock &	)	
Brown Infrastructure Limited, BBI US Holdings	)	DOCKET NO. D2006.6.82
Pty Ltd., BBI US Holdings II Corp., and BBI	)	
Glacier Corp. for Approval of the Sale and Transfer	)	
of NorthWestern Corporation Pursuant to a Merger	)	
Agreement	)	

Direct Testimony of

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on behalf of

**District XI Human Resource Council  
Natural Resources Defense Council  
Renewable Northwest Project**

December 2006

1    **Introduction and Summary**

2    Q.           Please state your name and occupation.

3    A.           My name is Thomas Michael Power. I am Professor of Economics and  
4           Chairman of the Economics Department at the University of Montana, Missoula,  
5           Montana. I am appearing in these proceedings, however, as an independent  
6           consulting economist on behalf of District XI Human Resource Council, the Natural  
7           Resources Defense Council, and the Renewable Northwest Project.

8    Q.           Have you previously testified before this and other regulatory commissions  
9           as an expert witness?

10   A.           Yes. I have testified before this Commission on numerous occasions over  
11           the past 30 years. I have also testified before federal and state regulatory  
12           commissions throughout the country on more than seventy occasions. A brief  
13           summary of my professional experience and training is attached as an appendix to  
14           this testimony.

15   Q.           On what issues will your testimony focus?

16   A.           My testimony will focus exclusively on the need to locate full control of  
17           NorthWestern Energy's (hereinafter "NorthWestern") Montana operations in  
18           Montana and not in Sioux Falls, South Dakota.

19   Q.           What conclusions do you reach in the testimony that follows?

20   A.           Let me simply list the conclusions that the analysis in the following  
21           testimony supports:

- 22           i. This Commission appropriately set Montana control of NorthWestern's  
23           Montana operations as one of the criteria to be met by anyone buying  
24           NorthWestern's Montana assets.
- 25           ii. The current arrangements that locates almost all of NorthWestern's top  
26           leadership in Sioux Falls, South Dakota, has seriously compromised utility  
27           decision-making in Montana.
- 28           iii. The Sioux Falls location of NorthWestern's corporate headquarters is a  
29           recent decision (1997) tied to NorthWestern's expectation that it would  
30           become a diversified national conglomerate corporation. That business  
31           strategy failed.

- 1           iv. Previous to adopting that strategy that led to bankruptcy, for almost 60  
2           years NorthWestern maintained its corporate offices in the geographic  
3           center of its South Dakota service territory, Huron, South Dakota.
- 4           v. With the purchase of the non-generating assets of the Montana Power  
5           Company and the shedding of its non-utility assets, NorthWestern's  
6           business center has shifted to Montana.
- 7           vi. Almost 90 percent of NorthWestern's profits are earned in Montana, almost  
8           90 percent of its electric sales are Montanan, 84 percent of its electric  
9           customers are Montanans, 75 percent of its employees are located in  
10          Montana, and two-thirds of its natural gas customers and sales are in  
11          Montana. Most of the risks to its profits are also associated with its Montana  
12          operations.
- 13          vii. Despite that overwhelming Montana focus of its business activities, 73  
14          percent of NorthWestern's corporate officers are located in Sioux Falls as  
15          are 60 percent of the corporate leaders who make decisions about Montana  
16          customers' default supply.
- 17          viii. This is a serious geographic mismatch that makes no business sense and is  
18          dangerous to the interests of NorthWestern's Montana customers.
- 19          ix. This Commission should condition its approval of the proposed BBI  
20          purchase of NorthWestern on either the movement of NorthWestern's  
21          corporate headquarters to Montana or the establishment of a truly  
22          independent, stand-alone, Montana company.
- 23          x. This is a perfectly reasonable condition. NorthWestern and BBI have  
24          already entered into an agreement with the South Dakota Public Utilities  
25          Commission to keep the corporate offices in South Dakota for three years.  
26          The Montana Public Service Commission should insist that either the  
27          corporate offices move to Montana at the end of that time period or that a  
28          stand-alone Montana company be established now.
- 29  
30  
31

1   **Personal Background**

2   Q.           The appendix that summarizes your qualifications indicates that you are  
3           an economist with considerable expertise in energy and utility regulation. Will  
4           your testimony in this case primarily consist of economic analysis?

5   A.           Only partly. My testimony will be based on my over thirty years of  
6           professional experience working with this Commission and this utility. My  
7           testimony will focus on my professional opinions as to what is necessary for both  
8           good utility decision-making and effective public regulation of utilities.

9   Q.           What is your background in working with the Montana Public Service  
10          Commission, Montana Power, and NorthWestern Corporation?

11 A.           In 1974 I was hired by the Montana Public Service Commission (MPSC) to  
12          analyze the need for the Colstrip 3 and 4 power plants and the likely impact on  
13          electric rates of incorporating those plants into Montana Power's rate base. The  
14          MPSC had a statutory obligation under the Major Facility Siting Act to comment  
15          on these issues.

16               In 1979 I began my almost 30-year relationship with District XI Human  
17          Resource Council. I prepared testimony for District XI on modifying residential  
18          rate design to both reduce the burden of electric rates on those who consumed  
19          relatively small amounts of electricity (including most low income households)  
20          while also encouraging more efficient use of electricity. Since then I have testified  
21          on behalf of District XI before this Commission around two dozen times.

22               In 1980 the Commission again hired me to develop testimony on  
23          appropriate PURPA avoided cost rates for qualifying independent generating  
24          facilities.

25               In 1987, in a negotiated settlement between District XI and the Montana  
26          Power Company that was associated with a rate case before this Commission,  
27          Montana Power Company committed itself to setting up a "Conservation and  
28          Least Cost Planning Committee" that would help guide the utility in its resource  
29          acquisition activities. I served on that Committee representing District XI.

30               As the regulatory issues facing Montana Power changed, the role of the  
31          advisory committee originally set up in 1987 changed too. This Commission  
32          incorporated that advisory committee into its regulations governing Montana

1 Power's resource planning and then into its regulations governing default supply  
2 planning and acquisition.

3 The advisory committee function continued with the transition to a  
4 restructured electric utility, default supply, and the purchase of the Montana  
5 Power transmission and distribution network by NorthWestern Corporation.  
6 NorthWestern, at various times, has had a Universal System Benefits Advisory  
7 Committee, an Electricity Technical Advisory Committee, and a Natural Gas  
8 Technical Advisory Committee. I have served on all of these advisory  
9 committees.

10 Q. What is the point of reciting this 30-year history?

11 A. I will be primarily drawing on that 30-year history of professional  
12 involvement with this Commission and this utility in my discussion of what I see  
13 as a prerequisite for the proposed merger of NorthWestern with the BBI holding  
14 company to be in the best interests of NorthWestern's Montana electric and  
15 natural gas customers.

### 17 **The Need for a Montana-Based Utility**

18 Q. What is the focus of your testimony?

19 A. The need to implement this Commission's earlier call for any company  
20 that wishes to take control of NorthWestern's Montana assets to have a Montana  
21 focus.

22 Q. How was that requirement been expressed by this Commission?

23 A. On October 14, 2004, this Commission unanimously adopted a set of  
24 guidelines entitled "Factors for Evaluating Proposals to Acquire Northwestern  
25 Energy." One of the requirements laid out in those guidelines was the following:

- 26 • "Demonstrable Montana focus
- 27
- 28 ○ Ideally, this would occur through a Montana headquarters of either the
- 29 company or a separate Montana utility subsidiary. A Montana
- 30 headquarters would reflect the relative importance of the Montana
- 31 operations and its long-term commitment to a successful Montana utility.
- 32 Based on Commission experience, management of the utility is most
- 33 effective when located where the company has the majority of its
- 34 business. Such a focus should certainly improve morale for employees
- 35 and result in better communications with the Commission.

- Ideally, there would be no operating ties to South Dakota or Nebraska. Sale of NorthWestern's operations in the other states would accomplish a Montana focus. An acceptable, but less preferable, Montana focus might also be achieved through a commitment of management, personnel and financial resources to the Montana operation.
- The Commission acknowledges economies of scale and scope, as well as sometimes more favorable access to capital that may be, but are not necessarily, associated with larger firms."

Q. Has your professional experience confirmed the "Commission experience" that "management of the utility is most effective when located where the company has the majority of its business?"

A. Yes. The contrast between working with NorthWestern Corporation and the Montana Power Company in an advisory capacity has been dramatic. With the Montana Power Company all of the management functions, including the top leadership, were located centrally in Montana. With NorthWestern's takeover of the non-generating assets of the Montana Power Company, decision-making within the utility appeared segmented and confused. Often employees in Butte, appeared to have limited authority. They appeared to be regularly taken by surprise by decisions made by NorthWestern leaders in Sioux Falls. Systematic decision-making seemed to collapse into an erratic stop-start-stop process that paralyzed decision-making for a time and then produced "emergencies" where decisions had to be made very quickly. The long and erratic course of obtaining long-term resources to support Default Supply is a good example. The Montana First Megawatts facility was in the mix, out of the mix, mysteriously back in the mix again, and then, just as mysteriously, permanently disappeared from the mix altogether.

Q. How did this stop-and-go decision-making affect NorthWestern's ability to make use of its advisory committees?

A. It largely ended effective and productive involvement of the advisory committees. No systematic work plan for the committees was ever developed. Meetings were irregular: At times of "emergencies" meeting might be scheduled weekly. Then we would not meet for months at a time. It was rare that

1 preparatory material was sent out enough ahead of time that committee  
2 members could think about or work on issues before the committee meetings. As  
3 a result, we were limited to “thinking off the top of our heads” and “shooting from  
4 the hip” when wrestling with relatively complex energy supply issues.

5 Q. Was it your experience that the separation of corporate offices in Sioux  
6 Falls and operational offices in Butte had an impact on NorthWestern’s ability to  
7 make use of its Montana advisory committees?

8 A. Definitely. The people making some of the key decisions were never  
9 present and, sometimes, the Montana personnel were not present either  
10 because they were back in Sioux Falls. There was regular emotional conflict  
11 between some of the Sioux Falls representatives and the advisory committee  
12 because the Sioux Falls folks did not understand the role of the committee,  
13 Montana regulation, or committee member’s past involvement with the utility.  
14 Some corporate decisions that Butte-based officers thought had been made  
15 appeared to be reversed in Sioux Falls. Some Sioux Falls decisions clearly did  
16 not understand conditions on the ground in Montana.

17 The net result of the division of authority was that the advisory committees  
18 could not be effectively engaged in assisting NorthWestern in its decision-making  
19 in a timely and productive manner.

20 Q. Have there been other worrisome changes in NorthWestern’s engagement  
21 with its advisory committees?

22 A. Yes. The range of issues that NorthWestern has brought to the advisory  
23 committees has narrowed considerably. The only partially-functioning committee  
24 currently operating focuses exclusively on some of the Default Supply issues. In  
25 the past there have been advisory committees dealing with low-income,  
26 Universal Systems Benefit, natural gas supply strategies, rate design, Qualifying  
27 Facilities, distributed energy policy (net metering, transmission and distribution  
28 cost savings, etc.), and legislative proposals. These remain important issues on  
29 which NorthWestern unavoidably has to and is making decisions. At this point  
30 NorthWestern is making those decisions without the assistance of any advisory  
31 committee involvement.

1 Q. Is this just a complaint that you and your colleagues on the advisory  
2 committees do not have as much influence on the utility as you did with the  
3 Montana Power Company?

4 A. Absolutely not. The Montana Power Company did not always or, even,  
5 usually take its advisory committees' advice. But that is not the point of the  
6 advisory committees. We are not the decision-makers; utility executive are. Our  
7 job is to help the utility test its ideas in a frank and critical setting so that the utility  
8 can improve its decisions. In the process committee members and their  
9 principals come to understand better why the utility makes the decisions that it  
10 does. All parties are better informed and, because of that, are more likely to  
11 make better decisions. It is not a matter of influence. It is a matter of  
12 systematically exploring together complex issues of mutual interest in the hopes  
13 of improving outcomes on the ground. It has been NorthWestern's inability to  
14 participate productively in that process that is worrisome. It is not a matter of  
15 egos, influence, or getting one's way. It is a matter of productively sharing  
16 information, opinions, and concerns.

17 Q. You paint a pretty grim picture of decision-making within and management  
18 of NorthWestern. Are you asserting that the entire corporation is dysfunctional?

19 A. Absolutely not. I have been focusing on two NorthWestern issues: Default  
20 supply decisions and interaction with its advisory committees.

21 NorthWestern has continued to provide reliable natural gas and electric  
22 service to customers in Montana. As far as I am aware, NorthWestern has  
23 managed and maintained the transmission and distributions system well.  
24 Although it took NorthWestern a relatively long time to put a long-term default  
25 supply portfolio in place, that job is almost finished. Fortunately NorthWestern's  
26 customers were not faced with another market "meltdown" like that in 2000-2001  
27 while NorthWestern, for many years, was primarily relying on market purchases  
28 to serve default supply customers.

29 NorthWestern has also played a very productive role on a variety of other  
30 fronts:

- 31 i. It has invested in favorably- priced, wind-electric generation that  
32 mitigates the significant price risk associated with future carbon



1 regulation and has been engaged in efforts to understand and  
2 manage integrating wind into the electric grid.

3 ii. It has expanded its efficiency and demand side management  
4 programs. However, with higher energy prices, there is more cost  
5 effective DSM available to be pursued and it could be pursued on a  
6 more aggressive schedule.

7 iii. It defended the USB program and all of its authorized public  
8 purposes while endeavoring to strike an appropriate funding  
9 balance among the various programs.

10 iv. It has supported, overall, low income programs during a period of  
11 rising market prices for energy focusing not only on low income  
12 discounts but also ongoing low income weatherization programs.

13 My impression is that NorthWestern, in most areas, has served Montana  
14 customer customers well since it took over the Montana Power non-  
15 generating assets.

16 That does not mean, however, that no further changes are needed  
17 within NorthWestern to protect the long-run interests of its Montana  
18 customers.

## 20 **The Geographic Structure of NorthWestern Corporation**

21 Q. Has NorthWestern in the past demonstrated that it actually agrees with the  
22 Commission's guideline quoted above that "management of the utility is most  
23 effective when located where the company has the majority of its business"?

24 A. Yes. From its founding in 1923 until 1997 the corporate headquarters of  
25 NorthWestern was located in Huron, South Dakota, not Sioux Falls. Huron is  
26 about 120 miles northwest of Sioux Falls but is located in the center of  
27 NorthWestern's South Dakota service territory. See the map below.



1  
2  
3 Q. Did NorthWestern choose the Sioux Falls location for its corporate  
4 headquarters because that city was more centrally located with respect to its  
5 South Dakota electric and natural gas operations?

6 A. No. NorthWestern provides no utility service in Sioux Falls. Sioux Falls is  
7 some distance from NorthWestern's core operations in South Dakota.

8 Q. Why then did NorthWestern's corporate headquarters get moved to Sioux  
9 Falls in 1997?

10 A. Beginning in the mid-1990s, Northwestern Public Service Company, the  
11 original name of NorthWestern Corporation, began an aggressive program of  
12 diversification through acquisitions away from being primarily a regional electric  
13 and natural gas utility. Like the Montana Power Company, NorthWestern wanted  
14 to move beyond the limited profits to be earned in the regulated utility business.

15 NorthWestern bought over 100, mostly small, companies in  
16 telecommunications, propane distribution, and heating, ventilation and cooling.  
17 These were consolidated into Expanets, Inc. that provided communication, data,  
18 and network services in 32 states, Corner Stone Propane Partners that was a  
19 retail propane distributor in 34 states, and Blue Dot Services Inc. that provided air  
20 conditioning, heating, plumbing and related services in 23 states. This nationwide

1 presence in these non-regulated industries contrasted with NorthWestern's  
2 regulated utility presence in just a small part of two states, South Dakota and  
3 Nebraska.

4 Having (temporarily, as it turned out) become a national corporation that  
5 made it into the Fortune 500, NorthWestern's top leadership decided it needed a  
6 more cosmopolitan corporate headquarter than Huron provided. In 1997 it  
7 shifted its corporate offices to Sioux Falls, the fastest growing of South Dakota's  
8 metropolitan areas, and in 1998 changed its name from Northwestern Public  
9 Service Company to the NorthWestern Corporation. NorthWestern provides no  
10 utility service in Sioux Falls. Its corporate headquarters were relocated outside its  
11 utility service territory.

12 Q. Does NorthWestern remain a diversified, largely non-utility business?

13 A. No. NorthWestern's diversification venture did not last very long. By the  
14 early 2000s only its utility operations were earning a profit and its far flung  
15 diversified ventures dragged NorthWestern Corporation as a whole into  
16 bankruptcy. Through the bankruptcy process it shed its failing non-utility  
17 businesses and emerged from bankruptcy largely an electric and natural gas  
18 utility again, with operations in Montana as well as South Dakota and Nebraska.

19 Q. What lessons do you see in this brief corporate history?

20 A. First, before NorthWestern launched its ill-fated diversification through  
21 acquisition adventure, it recognized the importance of locating its corporate  
22 headquarters in the center of its service territory. Northwestern serves both  
23 natural gas and electric customers in 59 communities in South Dakota. It serves  
24 only natural gas customers in just four communities in Nebraska. That geography  
25 led to the Huron location for its headquarters.

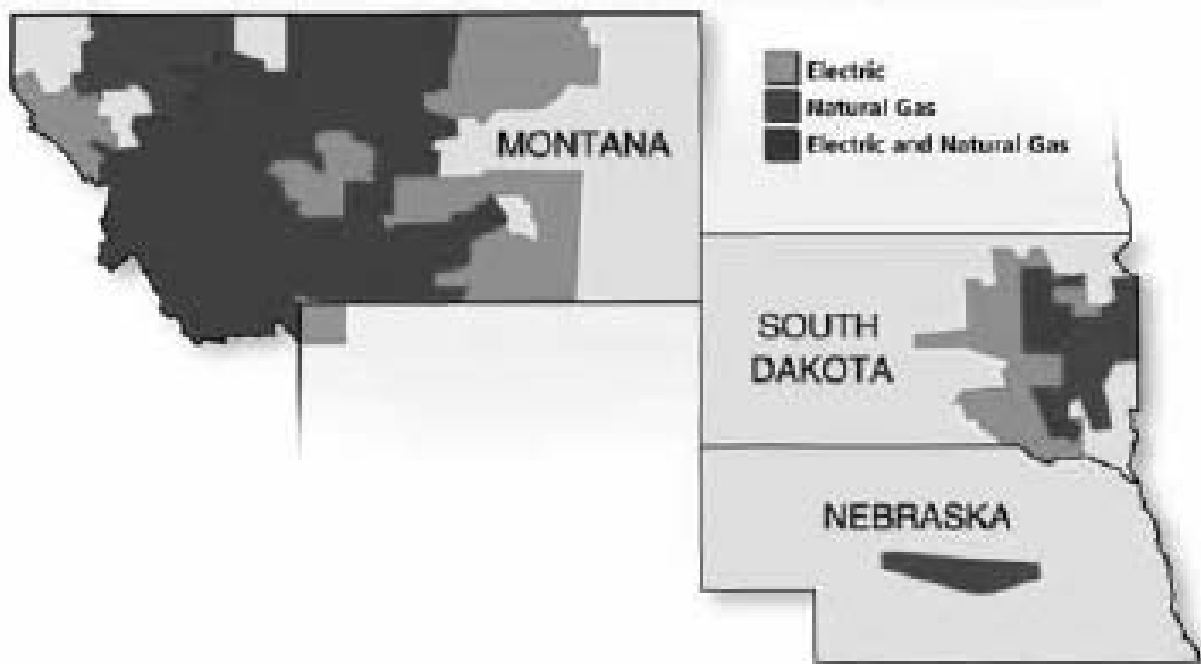
26 Second, the Sioux Falls corporate headquarters made sense only when  
27 NorthWestern was focused on becoming a non-utility business with holdings  
28 across the nation. The Sioux Falls location was not connected to its utility  
29 business. Given the catastrophic failure of NorthWestern's diversification  
30 ventures, the only logic the Sioux Falls location had has been lost. The Sioux  
31 Falls location is now an anomaly, a remnant of a misguided business adventure.

1 Third, given that NorthWestern is once again primarily a regulated utility,  
2 its corporate offices ought to be located where the bulk of its utility activities are  
3 located.

4 Q. Is NorthWestern now a geographically integrated utility serving contiguous  
5 service areas in South Dakota, Nebraska, and Montana?

6 A. No. As the map below indicates, NorthWestern's service territories in the  
7 three states are isolated from one another. As NorthWestern told FERC,  
8 NorthWestern's Montana and South Dakota electric transmission facilities are  
9 neither physically connected nor in the same North American Electric Reliability  
10 Council region. Similarly, NorthWestern's natural gas systems in Montana, South  
11 Dakota, and Nebraska are not connected. NorthWestern serves three separate  
12 and geographically-isolated areas.

### Electric and Natural Gas Distribution Service Area



13  
14 Q. What is the relative importance of NorthWestern's three separate service  
15 areas in its overall business operations?

16 A. Montana completely dominates the other two states. Montana is the  
17 source of approximately 90 percent of NorthWestern's before tax profits.  
18 Montana has close to 90 percent of electric energy sales, 84 percent of electric

customers, 75 percent of the employees, and two-thirds of natural gas customers and sales. Montana is now the business center of the NorthWestern Corporation. See the tables below.

<b>The Relative Geographic Importance of Montana Operations to NorthWestern's Profits: 2005</b>				
	Montana		South Dakota & Nebraska	
	Amount (\$ millions)	% of Total	Amount (\$ millions)	% of Total
Operating Income	\$ 130.7	83.7%	\$ 25.5	16.3%
Income before Taxes	\$ 99.8	88.5%	\$ 13.0	11.5%

Source: NorthWestern Confidential Information Memorandum, February 2006, Response to PSC-013(b), public version.

The Relative Geographic Importance of NorthWestern's Operations: 2004				
		Montana	South Dakota	Nebraska
Electric				
	Customers	310,000	58,200	0
	Peak Demand (mw)	1521	277	0
	Energy Sales (millions kwh)	8.9	1.1	0
Natural Gas				
	Customers <sup>1</sup>	166,800	41,500	41,500
	Energy Sales (million ft <sup>3</sup> )	21	5.1	5.5
Employees <sup>2</sup>		1,007	259	75
Percentage of NorthWestern Total				
Electric				
	Customers	84%	16%	0%
	Peak Demand (mw)	85%	15%	0%
	Energy Sales (millions kwh)	89%	11%	0%
Natural Gas				
	Customers <sup>1</sup>	67%	17%	17%
	Energy Sales (million ft <sup>3</sup> )	66%	16%	17%
Employees <sup>2</sup>		75%	19%	6%

1. Northwestern approximation that half of its SD and NE natural gas customers are located in each state.

2. The division of employees between SD and NE is approximate.

Source: 2004 10-K report to the SEC

1   **The Corporate Structure of NorthWestern**

2   Q.           How is NorthWestern's corporate leadership currently distributed  
3           geographically?

4   A.           According to the 2005 Annual Report (p. 15), NorthWestern has 15  
5           corporate officers. Eleven of them, 73 percent, appear to be located in the Sioux  
6           Falls corporate headquarters. The Sioux Falls officers include the:

7           President and Chief Executive Officer

8           Chief Financial Officer and Vice President

9           General Counsel and Corporate Secretary

10          Treasurer

11          Controller

12          Internal Audit and Control Officer

13          Vice-President for Information Technology

14          Vice-President for Customer Care and Communications

15          Assistant Corporation Secretaries (2)

16          Assistant Treasurer.

17          The Montana corporate officers include four vice-presidents: those for wholesale  
18          operations, retail operations, government and regulatory affairs, and  
19          administrative services.

20   Q.           Where are the officers who manage energy supply located?

21   A.           NorthWestern has set up an Energy Supply Board that has five members  
22           on it. Two of those, Pat Corcoran and David Gates, work out of the Butte office.  
23           The other three members of the Energy Supply Board, 60 percent of that Board,  
24           are based in Sioux Falls. The Sioux Falls members are corporate leaders to  
25           whom the Montana representatives report.

26   Q.           What conclusion do you draw from this geographic distribution of business  
27           activity and geographic distribution of corporate officers?

28   A.           The geographic distribution of officers is completely out of balance with  
29           the geographic distribution of business activity, profit potential, risk, employees,  
30           and customers. There is a serious mismatch.

1 **Proposals**

2 Q. What do you propose this Commission do about the geographic  
3 distribution of NorthWestern's corporate leadership?

4 A. This Commission should condition its approval of the BBI-NorthWestern  
5 merger on an agreement with BBI that within a relatively short period of time, say  
6 three years, NorthWestern's corporate offices would be moved to Montana. BBI  
7 was well aware of this Commission's guidelines for companies seeking to  
8 purchase NorthWestern's Montana assets. One of those guidelines was very  
9 explicit about corporate leadership being located in Montana.

10 Q. Why do you think that this is an appropriate condition to attach to the  
11 approval of the proposed merger with BBI?

12 A. NorthWestern's Sioux Falls corporate headquarters is a recent historical  
13 accident tied to a failed corporate diversification strategy. It makes no sense  
14 given the current and intended future focus of NorthWestern and BBI, namely on  
15 utility infrastructure and service.

16 The bulk of NorthWestern's business activities are located in Montana.  
17 Montana also represents the greatest risk to NorthWestern's profits both because  
18 some much of its business activities are located here but also because of the  
19 financial importance of default supply and the regulatory risks associated with not  
20 getting that right. Default supply is a not-for-profit service that NorthWestern is  
21 required by statute to provide. It earns no return on that activity, but it faces the  
22 risk of disallowance of tens of millions of dollars if it is deemed to have acted in  
23 an imprudent manner by this Commission.

24 NorthWestern, to thrive, needs to know Montana well: Its customers, its  
25 regulators, its governmental officials, and other stakeholders. It has to have its  
26 pulse on changing conditions, emerging trends, developing public opinion, and  
27 new opportunities. It cannot do that from a distant corporate headquarters that is  
28 physically removed from all of its service territories and 800 miles and most of  
29 the way across two large states from the business center of its operations. That  
30 simply makes no business sense.

31 Q. NorthWestern's CEO, Mr. Hanson, has said that the headquarters should  
32 stay in South Dakota because that is where the headquarters of NorthWestern

1 has been since it was founded (Response to MCC-16). Is this a convincing  
2 argument?

3 A. Certainly not. In 1997 Northwestern Public Service Company moved away  
4 from Huron, South Dakota, where it had been since its founding almost 60 years  
5 earlier, to Sioux Falls and changed its name. It did this in anticipation of being a  
6 diversified national corporation. Then, as that diversified company was failing, it  
7 bought the non-generating assets of the Montana Power Company. The  
8 abandonment of its non-utility holdings around the country combined with its  
9 purchase of the Montana utility properties shifted the center of NorthWestern's  
10 business to Montana. NorthWestern had a central reason to remain in South  
11 Dakota, amidst its electric and natural gas holdings, when it was primarily a utility  
12 serving part of South Dakota (and a tiny sliver of Nebraska). The business logic  
13 of that geographic location has been undermined by NorthWestern's own  
14 actions.

15 Q. NorthWestern's CEO, Mr. Hanson, says that any relocation of corporate  
16 headquarters from Sioux Falls to Montana "could cause a significant expense  
17 and disruption for South Dakota employees and their morale." (Response to  
18 MCC-16) How do you respond to that concern?

19 A. I suspect that Mr. Hanson is speaking for himself and his fellow Sioux  
20 Falls officers. They took their positions with NorthWestern understanding that  
21 they would be living and working in the Sioux Falls area. They are likely to have  
22 taken those jobs partially because they found Sioux Falls an attractive place to  
23 live. Since then they and their families are likely to have put down roots in that  
24 community.

25 However, corporate executives often have to change locations as they are  
26 promoted or their company reassigns them. Their preferences for locations  
27 cannot dominate business needs. If, for instance, the current officers had asked  
28 to live in Florida or Minneapolis while serving as officers for NorthWestern, they  
29 would not, hopefully, have been hired.

30 It is important to note that we are not talking about the relocation of most  
31 of NorthWestern's employees in South Dakota. Those focused on the operation,  
32 maintenance of South Dakota electric and natural gas facilities, providing South



1 Dakota customers with service, and interacting with South Dakota regulators  
2 would stay in South Dakota. We are only talking about the top leadership.

3 The Sioux Falls location was a mistake tied to a failed diversification  
4 strategy. With the abandonment through bankruptcy of those non-utility  
5 businesses, the business center of NorthWestern has shifted to Montana. The  
6 corporate leadership should follow.

7 Q. But is it not BBI's position that it wants to leave the existing structure of  
8 management in place?

9 A. Yes. That, in general, is its approach to managing its holding company.  
10 When it evaluates a company for acquisition, it also evaluates the management  
11 and only buys companies whose management it feels is doing a good job and  
12 will continue to do a good job. BBI wants to buy companies that can continue  
13 operating well with existing management.

14 In this particular context there is another reason for BBI's support for  
15 leaving the corporate headquarters in South Dakota. Because NorthWestern is a  
16 regulated utility, hearings such as this one before the Montana Public Service  
17 Commission have to take place in order to get approval for the proposed merger.  
18 BBI has to count on the enthusiastic support of NorthWestern's existing  
19 management in order to get that approval. That means that the desires of  
20 NorthWestern's corporate officers have to be supported by BBI.

21 There is no reason, however, why this Commission has to let those  
22 corporate officers' locational preferences dictate the continuation of a divided  
23 geographic structure of management that makes no business sense and is  
24 dangerous to the interests of Montana consumers. This Commission can insist  
25 on the ultimate relocation of corporate offices to Montana by conditioning its  
26 approval of the merger on obtaining such an agreement with BBI.

27 Q. Why do you suggest a three year period over which corporate leadership  
28 would relocate to Montana?

29 A. NorthWestern has already negotiated an agreement with its South Dakota  
30 regulators that commits NorthWestern to keeping its corporate leadership and  
31 support staff at levels "comparable" to those currently located there for three

1 years after the merger is implemented (Settlement Agreement, October 10, 2006,  
2 paragraphs 13 and 14).

3 This clearly indicates that NorthWestern and BBI think that the process  
4 used by regulators to approve the proposed merger is a legitimate venue in  
5 which to discuss and negotiate corporate office locations and staffing. That early  
6 agreement with the South Dakota Commission has put the Montana Commission  
7 in the position of allowing the “tail to wag the dog.” However, it would be  
8 disruptive to abruptly try to change the geographic location of corporate  
9 headquarters. That is likely to involve some employees choosing not to move  
10 with the relocation. Providing a several year process to plan that move and re-  
11 staff as necessary would have made sense in any case. For that reason, I do not  
12 see the agreement between BBI, NorthWestern, and the South Dakota  
13 Commission as blocking this Commission acting now to assure that ultimately  
14 NorthWestern’s leadership will move to the center of its business activity, namely  
15 Montana.

16 Q. What staffing is appropriately left in South Dakota?

17 A. I do not know the details of NorthWestern’s staffing in South Dakota. But  
18 NorthWestern has asserted that the operations and customer service functions  
19 for the South Dakota and Nebraska operations remained in Huron when  
20 corporate headquarters were moved to Sioux Falls. That is appropriate.  
21 NorthWestern would probably want an officer in charge of South Dakota  
22 operations (and possibly one responsible for Nebraska operations) to be named  
23 to serve a spokesperson within each state and to represent state employees’,  
24 customers’, and regulators’ concerns to top management. The idea is not to  
25 subordinate the South Dakota and Nebraska operations and leave them as “poor  
26 orphans” within the corporate structure. The point is to create a structure and  
27 geographic distribution of management that matches the structure and  
28 geographic distribution of business activity and risk.

29 Q. Is there an alternative organizational structure that would accomplish this  
30 Commission’s stated objective of having a Montana-focused and managed  
31 utility?

1 A. Yes. In fact, this Commission's "Factors for Evaluating Proposals to  
2 Acquire Northwestern Energy" suggest that alternative. That would be for  
3 NorthWestern to be broken into two autonomous pieces: The South Dakota-  
4 Nebraska operations and the Montana operations. After all, Northwestern Public  
5 Service Company successfully served its South Dakota and Nebraska customers  
6 for almost 80 years before the Montana operations were added to the corporate  
7 mix. Assumedly, the Northwestern Public Service Company could be resurrected  
8 as an independent company owned by BBI and the Montana Power Company  
9 name could be resurrected in Montana for an independent company also owned  
10 by BBI.

11 As this Commissions "Factors" pointed out, it is only potential economies  
12 of scale that justify combining these two operations. But given that there is no  
13 connection between the three geographically widely separated systems, it is  
14 likely that those economies of scale are quite small. Trying to run the Montana  
15 operations from the eastern edge of South Dakota also promises bureaucratic,  
16 communications, and political diseconomies. For that reason, a two-utility  
17 solution should also be considered.

18 Q. Does that conclude your pre-filed direct testimony?

19 A. Yes, it does.

## **APPENDIX**

### **Qualifications of Thomas Michael Power**

Q. What is your current employment?

A. I am a Professor of Economics and Chairman of the Economics Department at the University of Montana in Missoula, Montana, 59812.

Q. Please describe your formal education and training.

A. I received my Bachelor's Degree in Physics from Lehigh University in Bethlehem, Pennsylvania. I graduated with high honors and Phi Beta Kappa. I was elected a Woodrow Wilson Fellow in national competition and attended Princeton University where I received my Masters and Doctoral Degrees in Economics.

I taught math and physics at Lehigh University and have taught economics at Princeton University, Lehigh University, and the University of Montana. I have been on the faculty of the University of Montana since 1968. I have served as Chairman of the Economics Department since 1978. My specialties are regional economics and resource economics with an emphasis on energy, water, and environmental resources.

Q. Have you testified as an expert witness before utility regulatory commissions?

A. Yes. Since 1974 I have appeared before numerous federal, state, and municipal regulatory commissions.

I have testified before the Federal Energy Regulatory Commission, the Northwest Regional Power Planning Council, and the Bonneville Power Administration as well as before various congressional committees.

I have also testified before the utility regulatory commissions in the following states: Arizona, Colorado, Florida, Idaho, Indiana, Illinois, Kansas, Montana, Nebraska, Nevada, Oklahoma, Oregon, Texas, Utah, and Washington.

In addition, I have testified in utility cases before the City Councils of Seattle, Austin, and Spokane. I have also testified before the Snohomish County, Washington, Public Utility Board and the Springfield, Oregon, Public

Utility Board. I have testified in State District Courts in Idaho, North Dakota, Oregon, and Montana and in Federal Court in Montana.

I have testified before the Montana Board of Natural Resources and the Washington Department of Ecology, and the Washington Energy Facility Site Evaluation Council on the siting of energy facilities.

I have served as lecturer at National Association of Utility Regulatory Commissioners' Technical Conferences and at annual conferences of the Mid-America Regulatory Commissioners and the Western Utility Regulatory Commissioners.

Since 1988 I have served on the Montana Power Company Conservation and Least Cost Planning Advisory and Universal Benefits Advisory Committee. Since NorthWestern Energy Company took over the Montana Power distribution system, I have served on its Technical Advisory Committee and Universal Benefits Advisory Committee as well as its Natural Gas Technical Advisory Committee. For several years I also served on the Montana Regulatory Reform Working Group. In the past I have served on the Montana Governor's Citizens' Advisory Council on Energy. More recently I served on the Governor's Energy Security Task Force.

Q. Have you done other studies dealing with energy economics?

A. Yes. In 1975, I received an NSF/RANN grant to assemble a team of economists, geologists, and energy technologists to study coal development in the Northern Great Plains. That study led to a series of almost a dozen reports, the final summary being published as ***Projections of Northern Great Plains Coal Mining and Energy Conversion Development 1975-2000 A.D.*** Several of the other papers dealing with defining coal markets and energy projection techniques have also been published.

Between 1976 and 1985 I conducted studies of the economics of alternative energy systems, transmission reliability, the applicability of the PURPA rate making standards to hydroelectric system "going thermal", utility avoided costs, optimal operation of storage hydroelectric facilities, development of electric utilities on Indian reservations, and the impact of energy facility

development on local economic development. In 1995 **Public Utilities Fortnightly** published my article on "Making Sense of Peak Load Cost Allocations."

Q. Can you give examples of other studies have you done in the field of resource economics?

A. In 2001 Island Press published **Post-Cowboy Economics: Pay and Prosperity in the New American West**, which I co-authored with Richard Barrett. In 1996 two other books of mine were published. Island Press published **Lost Landscapes and Failed Economies: The Search for a Value of Place**. M.E. Sharpe published **Environmental Protection and Economic Well-Being: The Economic Pursuit of Quality**. The latter book is the rewritten and updated Second Edition of **The Economic Pursuit of Quality**, which was published by M.E. Sharpe, New York in 1988. I have also contributed two dozen chapters to various other books. Among the many articles and reports I have published are . "Public Timber Supply, Market Adjustments, and Local Economies: Economic Assumptions of the Northwest Forest Plan," (**Conservation Biology**, 20(2):341-350, 2006), "The Economics of River and Wetland Restoration in the Vermillion River Basin," **Great Plains Natural Resources Journal**, 4(2), Spring, 1999, "The Wealth of Nature," **Issues in Science and Technology**, National Academy of Sciences, Spring, 1996, "Economic Well-being and Environmental Protection in the Pacific Northwest," **Illahee: Journal for the Northwest Environment**, 11(3 & 4), Fall-Winter, 1995, and "Urban Disamenities" **Journal of Urban Economics**, June, 1981. In 1980, Westview Press published by book on **The Economic Value of the Quality of Life**. I have published papers on almost a dozen federal irrigation projects in the western states in addition to papers dealing with the value of in-stream flows for wildlife and recreational uses. I have testified before the State Board of Minerals and the Environment and the Oahe Conservancy Board in South Dakota as well as the Alberta Energy Resources Conservation Board and Natural Resource Conservation Board on topics related to resource development. I have also testified before Canadian Federal Environmental Review Boards.